MERGER DETAILS
AOL announced yesterday that it will merge with Time Warner, a leading media company, in a $350 billion stock transaction. AOL shareholders will receive 1 share of the new company to be called AOL Time Warner, while Time Warner shareholders will receive 1.5 shares of the new entity. AOL shareholders will own 55% of the resulting combination with closure of the deal expected by the end of calendar 2000. The transaction will be accounted under the purchase method of accounting with the goodwill amortized over a period of 20 years.

Companies mentioned: Time Warner (NYSE - TWX)
Excite@Home (NASD - ATHM)
Yahoo! (NASD - YHOO!)
Go Network (NYSE - GO)
Microsoft (NASD - MSFT)
Cisco Systems (NASD - CSCO)

* Banker Within the past three years, Bear, Stearns & Co. Inc., or one of its affiliates was the manager (co-manager) of a public offering of securities of this company and/or has performed, or is performing, other banking services, including acting as financial advisor, for which it has received a fee.

-> End of Note <-

-- FIRST CALL --

10:06am EST 11-Jan-00 Schroders (Newman/Davis 212-492-6658-6442) AOL TWX AOL.RV
AOL-TWX: Lowering AOL Target Price and Rating (1 OF 2)

Schroder & Co. Inc.
MORNING MEETING HIGHLIGHTS
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January 11, 2000

	AMERICA ONLINE (AOL -$71)	Rating: 2	Former: 1	
	TIME WARNER (TWX -$90)	Rating: 2	Former: 2	
ROE (2000E)	NA	Dividend	NA	
Tot. Debt/Cap (PF 2000E)	56%	Yie	NA	
PF Shares Out (mil.)	4,700	52-Wk	NA	
Proj. 5-yr. EBITDA Grow	20-25%	Book Value (PF 2000		$2.78
12-Month Target	$85 ($127 for TWX)	Fiscal Year	NA	
Price (Pro Forma)				
Market Cap.	$333 bil.			

	C1999	C2000E		C2001E	
		OLD	NEW	OLD	NEW
AOL EBITDA	$1,402	$2,167		$3,034	
TWX EBITDA	$6,110	$6,905		$7,816	
AOL TWX EBITDA PF	$7,512	$9,072	$9,072	$10,850	$11,350 (a)
EV/EBITDA			39.6x		31.7x

Includes $500 in synergies in calendar 2001.

HEADLINE: AOL-TWX; Lowering AOL Target Price and Rating; TWX Rated "2" Offers 18% Arbitrage Discount at Current Levels

INVESTMENT CONCLUSION: Yesterday, AOL (AOL) and Time Warner (TWX) announced a merger creating the world's largest media company and the only diversified media company positioned to hold a dominant role in the Internet. The merger will dramatically transform AOL and TWX, with AOL Time Warner having tremendous cash flow and greater earnings predictability, but much slower growth than AOL pre-merger. Accordingly, we believe valuation metrics need to be adjusted accordingly. Furthermore, arbitrage activity is likely to put pressure on AOL share value until the deal closes in about one year. As a result, we are lowering our 12-month price target from $105 to $85, which corresponds to 32x 2001 EBITDA, lowering our rating to "2" from "1," and removing AOL from our Recommended List. Our 12-month price target for TWX is $127 per share based on a fixed exhange ratio of 1.5 Newco shares/1.0 TWX shares.

KEY POINTS

Despite our enthusiasm for the transaction, we are lowering 12-month price target to $85 from $105, and correspondingly lowering our rating to a "2" from a "1," due to lower growth rate and transformation of AOL. The new company is

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clearly far different than AOL and therefore AOL's prior valuation metrics do not seem appropriate. We forecast EBITDA growth of 20%-25% (25%-30% in 2001 due to one-time boost from projected synergies). We arrive at our price target by applying a 32x multiple to our 2002E EBITDA. Additionally, we believe arbitrage is likely to pressure AOL's share price until the deal closes in about one year.

Cash flow powerhouse. We expect the combined AOL-Time Warner to generate EBITDA of over $11 billion in C2001, versus pro forma $9.1 billion in 2000E. Our 2001 figure includes our standalone EBITDA estimates of $3.0 billion for AOL and $7.8 billion for TWX as well as $500 million in synergies (management estimates $1 billion).

Unparalleled content. The merger combines TWX's cable, publishing and entertainment assets with AOL's ease of use, community, and proprietary content. This should drive the distribution of TWX's media assets online in a way that wasn't possible before, making the combined entity the unchallenged leader in terms of online metrics.

A solution to AOL's broadband worries. TWX's cable assets, with 21% of homes passed in the US, combined with the RoadRunner broadband service, provides AOL with a cable platform to complement its DSL strategy.

Spur demand for cable modems. From TWX's perspective having AOL as a partner should spur consumer demand for high speed internet access via cable. Road Runner currently has 450,000 subscribers.

Platform for international growth. Leveraging off TWX's international assets such as CNN, Time and People should enable AOL to speed up its international growth, which has been increasingly problematic.

Direct marketing opportunities to almost 100 million households. Beyond synergies created from the combined ad sales forces of the two companies, access to the subscriber bases of AOL's online service and TWX's HBO, Turner Broadcasting and Time assets provides huge opportunities for direct marketing. This benefit is significantly enhanced given the opportunities inherent in subscriber profiling.

Expanded merchandising opportunities. The merger boosts AOL's e-commerce opportunities, with such synergies as selling TWX merchandise and music online.

DISCUSSION

Deal Structure

Yesterday, AOL and TWX agreed to merge in an all-stock transaction. Each AOL share will be converted into one share of the new entity, AOL Time Warner, while each Time Warner share will be converted into one-and-a-half shares of the new entity. The acquisition will be accounted for using the purchase accounting method, with any resulting goodwill to be amortized over a 20-year period. Current AOL shareholders will control 55% of the new entity, while TWX shareholders will hold 45% of the company.

Financial Review of the Merger

* Over $40 billion in revenues in 2001E.
* Over $11 billion in EBITDA in 2001E, including synergies.
* Capitalization is clean with $17 billion in pro forma debt; 1.5x Debt to EBITDA ratio.
* Fastest growing diversified entertainment company.
* 30% of pro forma EBITDA from AOL growing at 40%-50%.
* 70% of pro forma EBITDA from Time Warner growing 12%-13%.
* Combined company should have long-term EBITDA growth of 20%-25% before synergies. Higher in 2001 (say 25%-30%) with synergies.

-- FIRST CALL --

* AOL Rated "2"
We have lowered our 12-month price target to $85 from $105, removed AOL from the Recommended List, and lowered our rating to "2" from "1." This merger is a major transforming event for AOL; clearly the new company bears only partial resemblance to the AOL predecessor. Thus, notwithstanding our enthusiasm for the transaction and belief that AOL Time Warner will be a media powerhouse, we believe we must conclude that AOL's prior valuation metrics no longer apply. While AOL Time Warner should have far more cash flow and earnings predictability than AOL, TWX's legacy businesses will slow EBITDA growth considerably. Thus, we project an organic EBITDA growth rate of 20%-25%, versus our prior estimate for AOL of 40%-50%. Accordingly, our prior multiples of nearly 200x 2001E EPS and 25x 2001E revenues appear hard to justify. Clearly investors will increasingly have to struggle with valuation metrics for traditional media/Internet hybrids.

On a pro forma basis, AOL Time Warner is currently valued at just under 40x 2000E EBITDA of $9.0 billion and about 32x 2001E EBITDA of $11.4 billion (which includes synergies). Assuming 20% growth our 2002E EBITDA would be $13.6 billion. Applying a 32x multiple to 2002E, which assumes no multiple expansion/contraction, and adjusting for debt and cash, we arrive at a 12-month price target of about $85 per share. We arrive at roughly the same value by applying a 38x multiple to 2001E EBITDA. If AOL Time Warner can achieve a higher growth rate, our valuation might prove too conservative, although there is little guidance for EBITDA multiples for Internet hybrids.

Beyond our valuation, arbitrage is likely to pressure AOL share price until the deal closes in about one year. We believe this further limits the near-term upside.

Table 1: Comparable Valuation Measures

Current Stock Price	AOL Time Warner $71	Time Warner Pre-Deal $65	Viacom CBS $59	Disney $36	Seagram $54
Projected EBITDA '00	9,072	6,905	5,290	4,462	2,575
Projected EBITDA '01	11,350	7,816	6,012	5,210	2,900
EPS+GW '00	0.67	1.50	1.28	0.83	1.45
EPS+GW '01	0.95	1.89	1.73	1.04	1.85
EV/EBITDA '00	39.6x	16.7x	20.6x	19.3x	13.1x
EV/EBITDA '01	31.7x	14.8x	18.1x	16.5x	11.7x
Price/EPS +GW '00	106.2x	43.2x	46.2x	41.3x	37.2x
Price/EPS +GW '01	74.6x	34.2x	34.0x	34.6x	29.2x
Proj. L-T EBITDA Growth Rate	20%	12-13%	15%	10-11%	9-10%
Proj. L-T EPS + GW Growth Rate	30%	20%	25%	15%	15%

TWX Rated "2"

-- FIRST CALL --

From the Time Warner perspective we are keeping the stock rated 2. We recognize that the stock price appreciation is about 40% based on the 1.5 exchange ratio for AOL Time Warner, which has a 12-month price target of $85 per share. Normally, we do not want to put a stock on the recommended list for less than 50% upside. However, the real reason for not upgrading the stock is one of perceived valuation risk, not that 40% appreciation is inferior. That does not imply that we are less than positive on the strategic implications of the deal. The question is simply how much is AOL Time Warner worth? Internet valuations have been in one world, and what we'll call, "more down-to-earth traditional valuations" in another world. They are now converging.

Therefore, looking at the combined company with about 70% of EBITDA coming from traditional media, there is some potential risk that the previous Internet valuation that AOL enjoyed may need to come down even further than the 38x multiple on 2001E EBITDA that we are assuming (see above). In light of this risk, we believe that TWX is better rated as a very strong "2" with a substantial arbitrage opportunity over the next year, assuming the deal goes through and AOL stock stays near current levels.

Broadband concerns addressed.
The merger will provide AOL with access to the second largest cable network in the US. Time Warner Cable, with 13 million subscribers, has about a 65% penetration ratio in the areas in which it operates. Overall, the company has 21 million homes passed, or 21% of the US market. By the end of 2000, it is expected that cable will be 100% upgraded to 750 Mhz, facilitating Internet access over cable and enabling the company to eventually offer such services as Interactive TV and IP telephony. These cable assets will complement AOL's DSL strategy and should provide additional leverage in its relationship with Bell Atlantic and SBC. The Road Runner broadband service, with 450,000 subscribers provides AOL with a near-term means of migrating some of its 22 million subscriber base to a broadband medium. Over time, we expect that the merger will spur growth in Road Runner's penetration and subscriber base.

-> End of Note <-

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AOL Time Warner has pledged to provide open access over its cable network. However, AT&T has made a similar pledge and it is clear that there are many different definitions of "open." Nonetheless, we believe AOL Time Warner will eventually gain access to AT&T's cable systems. With roughly 45% share of the dial-up market, AOL is well-positioned to compete in the broadband environment, through cable, DSL, and satellite.

The merger also boosts AOL's effort in providing Internet over television. We believe this market could potentially rival high-speed Internet over PCs. However, we believe it requires a different kind of content, as well as access to cable networks. With its broadcast, Internet, and cable assets, AOL Time Warner could be a leader in delivering this type of next generation interactive programming.

Combined assets create a content behemoth.
AOL has built its popularity on the basis of content, community, and ease-of-use. With the growth of the Internet, AOL's content edge has been diminished. However, TWX brings some of the best brands in media and entertainment. We see several implications. AOL has been a leader in developing Web properties. It could revitalize the Web presence for TWX's leading properties. However, we note that TWX's properties already rank ninth in terms of reach (November 1999, Media Metrix). AOL is facing challenges from free ISPs. While community/chat and ease-of-use provide strong differentiation, AOL could now add proprietary content. For example, certain TWX assets such as Business Week, have additional Web content that is available only to subscribers. This access could be extended to AOL subscribers as well. AOL's international expansion has also been struggling. We believe this is due, in part, to limited international content and free services. TWX's global brands could help boost AOL's value proposition.

Peeking into the future, one can envision such synergies as the provision of Warner Bros. content through AOL interactive television services over Time Warner cable lines. IP telephony to AOL subscribers is also a likely synergy that the companies will seek to implement. Through broadband, the company could even offer IP-based MP3 subscriptions to its music libraries.

With a plethora of subscription services, AOL Time Warner gains tremendous pricing flexibility. Subscribers will choose among cable, premium cable, broadband Internet, Internet over TV and other devices, magazines, eventually telephony, and other services.

Industry Implications
Internet: We believe that this merger is likely to have significant long-term implications for other online companies and may drive a number of copycat mergers between Internet and media companies.
* Yahoo! (YHOO, "2" rated) remains the premium Internet pure-play. Yahoo! has indicated that it wants to be distribution independent, so it can work with all potential partners. In this light, and given its lofty valuation, YHOO is seen as less likely than some of its competitors to initiate a merger with a media company.
* Excite@Home (ATHM, "1" rated") comes out of this announcement slightly better

than would otherwise be expected. Although ATHM's Excite network falls far short of AOL Time Warner in terms of content, the merger portends well for ATHM's @Home broadband connectivity business. The deal does not hurt ATHM's exclusive access to its cable networks; although it appears that it will give ATHM access to TWX's cable networks, given AOL and Time Warner's commitment to open access. Furthermore, despite AOL's mass market efforts, a substantial portion of the online population have chosen to look elsewhere for their Internet connectivity. If not for its complication exclusivity contracts and AT&T approximately 25% stake, we would consider ATHM a more likely merger partner.

* Lycos (LCOS, "2" rated") is a willing merger partner for a major media company, given its relatively modest market capitalization of $8 billion, compared with YHOO's $129 billion. More than any of the other top online networks, LCOS needs a media partner to help it drive reach and stickiness.
* Go.com (GO, "1" rated") emerges from this deal as a prescient combination of a major media company with an online network. The AOL-TWX deal certainly validates Disney's acquisition and integration of GO with its own online assets.
  GO falls short of the combined AOL-TWX in terms of connectivity (i.e. TWX's cable assets and AOL's online subscriber base); but it does have a major broadcast network, which far surpasses TWX's WB network.

* Diversified Entertainment:
The question is which entertainment companies will be under pressure to do a similar deal? The market is full of speculation.
* Within our universe of coverage there are three possibilities (all of which bounced yesterday): Viacom, Disney and Seagram.
* Which are the most attractive merger candidates? Three things are important: 1) content, 2) high speed internet distribution, and 3) broadcasting and/or cable networks to cross-promote the brands. Time Warner had all of the above. Viacom and Disney have #1 and #3. Seagram has #1.
* Viacom - we believe the most likely to do a deal (as long as Sumner retains voting control), yet even without that speculation still very attractive on a fundamental basis. Rated 1. Buy it.
* Disney - least likely to merge. Two reasons: 1) the psychology of accepting a currency based on Internet valuations may be a hurdle, and 2) the progress the company has already made in Go. Speculation may continue, but we don't expect a deal. Still rated "3" based on the fundamentals.
* Seagram - could do a deal, which would likely require splitting up the company between spirits and entertainment. Not as compelling a partner as Viacom/CBS, but still has valuable content, especially as a play on Internet opportunities for music. Strong story without a deal. Buy it in addition to Viacom and Time Warner. Rated 2.

* Regulatory issues
The deal is subject to regulatory approval at a number of levels. The Justice Department will address antitrust issues relating to the merger and the FCC may get involved. Additionally, transfer of Time Warner Cable's cable licenses to AOL will need the approval of local authorities. We believe that part of the reason for the long time frame of the merger is the complexities expected in obtaining approval from all of these regulatory bodies. We believe that the commitment to open cable access is likely to make the passage of the merger easier as local municipalities will not be faced with the same issues that have caused several of them to prevent the transfer of TCI's cable licenses to AT&T.

-- FIRST CALL --

08:37am EST 11-Jan-00 Jefferies & Company, Inc. (Frederick W. Moran (212) 284-
AOL-Buy: America Online, Inc. First Integrated Internet, Media &...

** JEFFERIES **** JEFFERIES **** JEFFERIES **** JEFFERIES **** JEFFERIES**

America Online, Inc. (AOL) - $75 1/8*

Frederick W. Moran (212) 284-2262
Jeffrey C. Cino (212) 284-2390

First Integrated Internet, Media & Communications Company

Rated Buy

52 Wk Range	$96 - $24	FY Jun	1999	2000E	2001E	2002E
Shares Out -FD(MM)	2,460.0	1Q	$0.02	$0.07A	$0.11	$0.15
Float (MM)	2,337.0	2Q	$0.04	$0.08	$0.12	$0.16
Insider Own	5%	3Q	$0.04	$0.09	$0.12	$0.17
Equity Mkt Cap (MM)	$184,808	4Q	$0.06	$0.09	$0.13	$0.20
Total Ent.Value (MM)	$185,053	EPS	$0.17	$0.33	$0.48	$0.67
3-Yr Rev Grwth Rt	30%	P/E	NM	NM	156.7x	110.7x
3-Yr EPS Grwth Rt	60%	EBIT	$577	$1,217	$1,885	$2,651
		Revenue	4,777	6,560	8,351	10,332
		EV/Rev	NM	28.2x	22.0x	17.7x

Figures represent pre-goodwill EPS
*Intraday pricing
($MM), except per share data

Our rating on America Online shares is Buy and our 12-18 month price target is $110. This morning, America Online and Time Warner announced an all-stock merger of the two companies valued at roughly $350 billion to create the world's first fully integrated Internet, media and communications company. The deal should be viewed favorably for AOL as it combines the leading online services company with the leader in branded content, providing for tremendous advertising and commerce opportunities; it secures AOL's access to high-speed broadband cable pipes; and it uncovers tremendous cross-selling and cross promotion.

First Fully Integrated Media and Communications Company - This morning, America Online and Time Warner (TWX - $92, Buy) announced an all-stock merger of the two companies valued at roughly $350 billion to create the world's first fully integrated media and communications company.

Combined Company at a Glance - Based on our calendar year 2001 estimates for the separate companies, we believe the combined entity could generate total revenues of $41.7 billion and EBITDA and operating income of $10.7 billion and $7.3 billion, respectively, excluding synergies. Combined net income on the same basis would be $3.0 billion or $0.63 per share, which indicates that the deal should be accretive to AOL's fully diluted recurring EPS by $0.03 in calendar 2001.

Huge Advertising and E-Commerce Opportunities - The merger combines leading online functions with leading branded content and should drive significant advertising and e-commerce opportunities. With an unparalleled audience reach consisting of over 100 million paid subscription relationships, we believe the company will benefit from huge advertising and e-commerce relationships.

Cable Broadband High-Speed Access - The deal provides the long awaited answer to the open-access debate, securing AOL's access to broadband cable pipes via Time Warner's RoadRunner broadband cable Internet service. Time Warner currently serves over 13 million cable subscribers, roughly 427,000 of which already subscribe to the high speed RoadRunner service.

Exchange Ratios - America Online shareholders will receive 1.0 share of the new company for each AOL share and Time Warner shareholders will receive 1.5 shares of the combined company for each TWX share on a tax-free basis. AOL shareholders will own roughly 55% of the new company and Time Warner shareholders will receive 45%. The merger will be accounted for as a purchase transaction and is expected to close at the end of calendar 2000.

New Management Structure - AOL's CEO Steve Case will serve as the new company's Chairman and Time Warner's CEO Gerald Levin will be the combined company's CEO. Time Warner Vice Chairman Ted Turner will be Vice Chairman of the new company. AOL and TWX President's Bob Pittman and Richard Parsons will be co-Chief Operating Officers and AOL CFO J. Michael Kelly will be the new company's CFO and Executive Vice President.

Other Stocks to Benefit - We believe other stocks that could benefit from the AOL Time Warner announcement include Yahoo! (YHOO - $440 1/2, Buy), Lycos (LCOS - $76 3/8, Buy), Viacom (VIAB - $56 7/8, Buy) and Disney (DIS - $34 7/8, NR), as they are all potential candidates for similar deals.

Combined Company

Based on our calendar year 2000 estimates for the separate companies, we believe the combined entity would generate total revenues, EBITDA and operating income of $437.3 billion, $8.6 billion and $5.5 billion, respectively, excluding synergies. Combined net income on the same basis would be $1.9 billion or $0.42 per share, accretive by $0.02 to our current calendarized 2000 EPS estimate. Once the merger is completed, we believe it could generate total revenues of $41.7 billion and EBITDA and operating income of $10.7 billion and $7.3 billion, respectively, excluding synergies. Combined net income on the same basis would be $3.0 billion or $0.63 per share, which indicates that the deal should be accretive to AOL's fully diluted recurring EPS by $0.03 in calendar 2001.

Fiscal 2Q00 AOL Estimates

We believe AOL should evidence powerful subscriber growth through the seasonally strong winter months, combined with continued momentum from PC rebate deals that have been offered through the holiday season. In the second quarter of 2000, we expect the company to record 22.7 million total subscribers including both the core AOL premium brand and the CompuServe value brand. This estimate represents 33% year-over-year growth based on 1.7 million net additions. Our U.S. AOL-branded subscriber estimate of 17.5 million represents 32% growth based on almost 1.3 million net additions and our AOL International JV subscriber estimate of 2.7 million indicates 48% growth, including 244,000 net additions. Thus, total AOL-branded subscribership should climb to almost 20.2 million. As CompuServe's U.S. operations target value customers, we expect subscriber growth to ramp up to record levels, maintaining the momentum established in the June quarter through $400 PC rebate deals with eMachines. We expect that CompuServe should add 232,000 U.S. subscribers in the December quarter, increasing the total count 42% to 1.7 million. Our CompuServe European JV subscriber estimate is 765,000, a slight decline from the prior quarter, as the company develops a strategy to prevail in a market currently dominated by free ISPs.

Total revenue, comprised of subscription, advertising and commerce, and enterprise revenue, should increase 40% to $1.6 billion, driven primarily by growth of the company's core AOL brand and impressive advertising and commerce opportunities. Gross margin should improve 190 basis points from the prior year and 10 basis points from the prior quarter to 46.2% as the company continues to scale down network costs. AOL-branded online service revenue should increase 40% year-over-year to $1.0 billion, based on continued industry-leading subscriber growth and steady, industry-leading monthly revenue per customer. CompuServe-branded revenue should come in at $51.1 million and our enterprise revenue estimate, which reflects Netscape's fully integrated enterprise software and service unit, is $124 million. Our advertising, commerce and other revenue estimate stands at an impressive $415 million, representing 70% year-over-year growth. This powerful growth is based on several factors, including: industry-wide growth of online marketing spending; strong e-commerce opportunities during the holiday shopping season; and AOL's industry leading position, multiple brands and broad consumer reach across a vast number of online eyeballs through its multiple leading brands. For the December quarter, we expect EBITDA to increase 86% year-over-year to $410 million and operating income to increase 128% to $185 million. Fully diluted recurring EPS should be $0.08.

Fiscal 2000 Estimates

In 2000, we expect the company to record 30% growth to 25.4 million total subscribers based on 5.9 million net additions including both AOL and CompuServe. Total revenue, comprised of subscription, advertising and commerce, and enterprise revenue, should be $6.56 billion, a 37% YoY increase. We expect gross margin to increase 170 basis points versus the prior fiscal year to 46.2% as the company continues to scale down network costs. We expect EBITDA growth of 79% to $1.7 billion and operating income growth of over 110% to $1.2 billion. Our estimates indicate an impressive operating margin improvement of 650 basis points YoY to 18.6%. We expect fully taxed net income growth of over 110% to $838 million or $0.33 cents per diluted share.

Description

America Online, Inc. stands as the world's largest Internet and online service provider, boasting some of the most powerful brand names in the online world. The company has captured tremendous growth, aggregating nearly 21 million estimated current total AOL members globally including CompuServe. The company continues to enhance its branding through promotion of its core AOL brand as well as through the development and acquisition of other Internet brands such as ICQ, AOL Instant Messenger, Digital City, CompuServe, Netscape, AOL MovieFone, Nullsoft, Spinner and AtWeb. Through a strategic alliance with Sun Microsystems (SUNW - $76 1/8, NR), the company offers end-to-end e-commerce and enterprise solutions to business customers.

For a complete version of this note which contains tables and/or graphs,

-- FIRST CALL --

08:45am EST 11-Jan-00 SG Cowen Securities Inc. (REAMER, SCOTT 212-495-7769) AOL
AOL/THE MOTHER OF MERGERS CREATES A...ER...UMM...COMPANY THE...PT.1/STRONG BUY

SG COWEN
Scott Reamer
212.495.7769
January 11, 2000

PART 1 OF 2

America Online (AOL: $73
RATING: Strong Buy (1)
The Mother Of All Mergers Creates A...Er...Umm.A Company The Street Has Never Seen Before

==

	AOL EPS (FY Jun)			AOL Quarterly EPS				
	EPS	Revision	P/E	Q1	Q2		Q3	Q4
F98A	0.03		NM	0.01	(0.01)	0.01	0.03	
F99A	0.17		NM	0.03	0.04	0.05	0.07	
F00E	0.33E		221x	$0.07	$0.08	$0.08	$0.10	
F01E	0.55E		133x					

Market Cap: $ 172 billion. Note:above do not reflect merger with Time Warner

Please see a related note published today by SG Cowen's Media analyst Ed Hatch who covers TWX

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Key Points:

1. AOL and TWX announced they will merge in a stock for stock purchase transaction valued at $350 billion.
2. The rationale and logic seem to make lots of sense to us: revenue leverage and cost savings via the combination of AOL's distribution prowess and TWX's content brands; AOL Time Warner will have over 100mm paid subscription relationships with consumers.
3. The commerce possibilities alone could have powered the deal: music, video, films; all can be sampled, viewed, and owned with three short clicks.but that's not all
4. TWX's cable plant clearly gives AOL much-needed cable plant access for broadband, but equally important longer term is the potential telephony play over that network. AOL's ICQ/AIM/Buddy Lists and ownership of a 100% digital network last mile? What works for AT&T should also work for AOL Time Warner
5. Keeping the Strong Buy on AOL thanks to the underlying logic of the deal and the likelihood that both the combined model ($2.40+ EBITDA per share `01) and the existing valuation of the combined entity (35Xs '01 EBITDA) are conservative. We look for both greater long term EBITDA margin and a greater understanding of the uniqueness of this company in the public markets to drive the stock toward 2H:00. Till then.hang on.

Investment Thesis:
We have long been unrepentantly bullish on AOL based on our belief that the Street would come to understand both the potential of this new medium as well as AOL's dominant place within it. We still believe that the Street is under-estimating the value of AOL's two most important corporate assets:

-- FIRST CALL --

its pre-eminent online brand and its massive subscriber (read: use) base. Both of these are, by all indications, growing stronger with each passing quarter. Combine these assets with Time Warner's content and cable distribution assets, and you're looking at a company whose ability to monetize those brands and that consumer footprint is unrivaled on the Street. The value of the combined AOL/TWX entity will ultimately be determined by their ability to drive revenue from this consumer influence: our bet continues to be that it's quite a bit higher than these levels. The true earnings power of this model should come into view over the next few quarters, as AOL and Time Warner highlight the new products, services, and revenue streams available to it they didn't have before. For now, we'll continue to focus on the four key, manageable elements of the AOL model (sales and marketing expenses, advertising and commerce revenue, gross margins, and subscription revenue). And though we're wary of sounding too much like sycophants on a stock that has had such a tremendous run, but we really do believe that AOL Time Warner is well on its way to becoming the next great (big) Internet media/commerce/communications company of the future. AOL should be a core technology holding.

Discussion

Lots Of Breathless Enthusiasm And Lots Of Handwringing, But What's The Elevator Message?
Yes, we're on board about the importance and value of AOL's Internet distribution prowess; we agree that TWX's leading content will create greater revenue at lower costs distributed on AOL's properties; we understand the logic of the advertising/commerce/subscription revenue leverage; we can clearly see the importance of AOL having access to TWX's cable plant; and we get the cost savings of having one ad sales force and by cross promotion of in-house properties. All of these points have already been and (and no doubt will continue to be) poked, prodded, and generally kneaded into mental submission. What we're focused on post merger is the same thing we were focused on pre-merger: AOL as "the next great (big) Internet media/commerce/communications company of the future" as our above description has stated. So what's the TWX merger's impact on that statement becoming a reality? Big.

Remember Our AOL-As-Internet-Telecommunications Company? TWX Advances That Nicely
We've spoken at some length that we think that the ultimate value of AOL is a function of the number of consumer relationships they have at at what level they would be able to monetize them. O fcourse, AOL's ability to monetize those consumer relationships have had as their fulcrum the advertising/commerce deals AOL has been able to sign. To a large degree AOL has been viewed as an Internet media and commerce company, whose revenue was levered against these two revenue streams. Increasingly over 1999, we've called on the Street to view AOL also as an Internet telecommunications company whose telecomm assets (AIM, ICQ, Buddy Lists) remain under appreciated by investors and under levered by the company. Our original bullish call on this name had that thesis as its foundation.

What Works For AT&T Should Work For AOL/TWX
And as everyone is clearly aware by now, the AOL/TWX merger gives AOL access to 20mm households passed (13mm subscribers) with 100% digital upgraded plant by the end of 2000. This suggests that, not only will AOL

be able to offer a cable broadband service that is competitive and broad, they will also be able to offer, potentially, telephony services over that same digital infrastructure, using their consumer base and telecom applications (AIM, ICQ, Buddy Lists) as the consumer hooks for that service. So in one fell swoop, AOL puts a wooden stake in the heart of the broadband issue that has plagued them and simultaneously, has the capability to deliver telephony service across that same infrastructure. After all, if it woks for AT&T (who is hoping to offer local, long distance, cable, and Internet access over one network), why wouldn't it work for AOL? And though you'll hear from us on the very many revenue synergies and the sizable cost savings over time for the combined companies, our telescope is still (more than ever in fact) fixated on trying to discern when AOL's prospects start to reflect the vast telecommunications opportunities that lie before them. The TWX merger in our eyes only reinforces this thesis.

And Keep In Mind The Marketing Budget The Combined Company Is Going After
AOL Time Warner is going after a much bigger market in terms of sheer dollars than traditional advertising budgets. Assume for instance that traditional advertising (including direct mail) represents a $200 billion opportunity. However, the dollars that AOL Time Warner had the potential to garner is much greater than just traditional advertising dollars and here's where the market really expands. Over $100 billion is spent on telephone marketing, $80 billion on promotions, $3 billion on market research and $59 billion on trade shows. All in these non-traditional advertising dollars represent $242 billion and all are available to AOL's/TWX's combined ad sales force.

You Know The Specifics, But If You've Been Asleep For The Last 24 Hours, Here Goes
Early yesterday morning AOL and TWX announced a merger of equals in a stock-for-stock transaction valued at roughly $350 billion. The merged entity will be named AOL Time Warner. Under the terms of the merger, each AOL shareholder will receive 1 share of AOL Time Warner, and TWX shareholders will receive 1.5 shares of the newco (the exchange ratio is fixed and there is no collar). The transaction, which is expected to close by year-end (subject to HSR and other regulatory approvals), will be accounted for as a purchase. Upon closing, AOL Time Warner will have roughly 4 billion shares outstanding, with AOL shareholders owning approximately 55% of the combined entity.

So What's A Model Look Like?
As an exercise in possibilities (and with no guidance from the companies whatsoever), we put together a potential model of the combined entities below that, among other things, illustrates the potential EBITDA creation this entity could achieve.

AOL/TWX	1998	1999	2000E	2001E	2002E	2003E	2004E
TWX Revenue	26.2	27.5	30.0	33.1	36.5	40.1	43.7
% change	--	4.9%	8.8%	10.4%	10.3%	10.0%	9.0%
AOL Revenue	2.3	3.8	5.7	8.0	10.8	14.0	17.9
% change	--	66.0%	48.0%	40.6%	35.0%	30.0%	27.5%
Combined Revenue	28.6	31.4	35.6	41.1	47.3	54.2	61.6
% change	--	9.9%	13.6%	15.2%	15.1%	14.6%	13.8%

-- FIRST CALL --

Combined EBITDA	5.8	6.5	7.5	9.6	10.9	13.4	17.6
margin	20.4%	20.6%	21.1%	23.4%	23.0%	24.8%	28.5%
% change	--	11.0%	16.3%	27.8%	13.3%	23.6%	30.7%
Shares	--	--	--	4	4	4	4
EBITDA/Share	--	--	--	$2.40	$2.72	$3.36	$4.39

How Does This Transaction Impact The Rest of The Industry?
Obviously a number of companies will be affected by such a transaction. Here we briefly run down the Top 20 Internet companies on a market cap basis and how they are affected by the deal:

YHOO: Could lead to a partnership with a traditional media company - many of the same technology, brand and consumer touch points exist - although YHOO has no subscription relationship with consumers.

AMZN: AOL/TWX partnership will have enhanced and greater commerce opportunities, however we don't believe the Internet's #1 retailer is reeling from this announcement. But keep in mind that AOL Time Warner does have 19mm music customers, 16mm from Columbia House membership and 3mm CD Now customers. As well, AMZN and AOL have an existing advertising relationship.

AKAM: CNN Interactive is a customer for content delivery.

EBAY: Multi-year, multi-million dollar agreements with AOL.

-> End of Note <-

ATHM: The Excite@Home merger was viewed as the original media/distribution agreement in the Internet age. However, things have been rather slow in panning out - ATHM subs are just north of 1mm (reached the 1mm milestone on 12/6/99) and Excite@Home reached 15mm unique visitors in Nov (acc to Media Metrix). Throw in another 13mm from the BlueMountain Arts acquisition and it's still under 30mm. What differentiates the AOL/TWX deal so much from XCIT/ATHM is the fact that both AOL and TWX have large subscriber bases. We believe it will be easier to upsell a subscriber or bundle additional services than it is to cross promote a subscription service on a free service.

RNWK: Has a relationship with Road Runner.

DCLK: TWX is one of the largest direct marketers in the world and one of Abacus Direct's biggest clients (which means they are now one of DCLK's largest data clients). We think the combined company (AOL/TWX) has an even greater need for data than on a stand-alone basis.

Other Derivative Plays
The table below is a chart of over 70 companies that have deals with AOL that in some fashion could be enhanced by the combined companies' content and distribution assets.

A Sampling of Companies That Have Deals With AOL

Wal-Mart	Circuit City	Medscape	UA Theaters	eBay	Blockbuster	Toys R Us	Dr. Koop
Stamps.com	Gateway	Travelocity	Maketwatch.com	Intuit	The Gap	Lanac.com	Careinsite
Netmarket	Lotus	Novell	Financial Engines	Lycos	Compaq	HP	Inktomi
Earthlink	Ameritech	Net2Phone	1-800 Flowers	Juno	GemStar	Emachines	iTurf
Emusic.com	Real Select	MamaMedia	Weather Channel	GTE	Planet Rx	Tel Save	CBS
Videos Now	Time Inc.1	Digital Chef	Big Entertainment	IBM	BOL	Sony	Liquid Audio
Scudder	InfoSpace	MetroCall	Hughes Electronics	NPR	N2K1	Amazon	DVD Express
PBS	Casio	The Knot	New Line Cinema1	iOwn	Bank One	Citibank	CBS Sportsline
Wells Fargo	B of A	Autoconnect	Columbia House1	Tivo	Etoys	Acer	General Motors

1Refers to TWX owned properties.

In addition to the companies listed above, InterVu has an equity investment from CNN, as well as operational relationships with Warner Brothers, Turner Broadcasting and CNN.

The Consumer Footprint Is Enormous
On an albeit rough estimate, the figures for consumer footprint for each of

the various properties are laid out below. On a subscriber basis, the combined company has more than 100mm paid subscription relationships (those numbers are in bold below)

AOL Assets		TWX Assets	
AOL	20mm subs	Cable Systems	13mm subs (20mm homes passed)
CompuServe	2.2mm subs	HBO	35mm subs
Int'l	3.4mm subs	Cable networks	75mm users (CNN 1B
NSCP	20mm users	Film	265mm domestic (18% mkt share)
ICQ	50mm users	Publishing	28mm subs (120mm users)
AIM	50mm users	Books	4.1mm subs
MovieFone	1.2mm	Music	16mm subs - CH
DCI	6mm		3mm - CDNW cust
Spinner/Winamp	10mm	WB	4.5mm users
AOL.com	44mm	Film	265mm domestic (18% mkt share)

As For Price Target And Valuation.We'll Defer For Now
The debate that is likely to rage on the Street over the next few months will be focused on just what valuation methodology should be applied to the combined entity. Revenue multiple? Doesn't account for the cost structure of the company. Earnings multiple? Doesn't account for the D&A elements now part of the combined entity. EBITDA Multiple? Cash Flow Multiple? Free Cash Flow? All have their merits and demerits, though we personally are coalescing around a Cash Flow Multiple as the right way to value this thing. That, however, is only one part of the battle: determining what multiple will be as important as determining the methodology. Should it be based on historical media company multiples or something significantly higher? We've asked more questions than we've answered because we're still noodling on this one ourselves. After all, we're talking about a company whose financial profile has no precedent (at least if you believe the stated synergies and we do).

The Stock, However, Could Very Well Tread Water For A Spell But That Doesn't Change Our Rating
The old saw that acquirors overpay, that synergies are fleeting, that half of all mergers fail, the skepticism behind the purchase vs. partner logic, and the relative information vacuum all could produce a "digestion" period that could last for a few months and that could keep the stock range bound. We believe that by the middle of the year, we could see material new announcements from AOL and Time Warner that further describe the revenue synergies available to the company post merger. Till then, we're not likely to see much in the way of significant new news that will help investors gauge (with any greater clarity) the logic of this transaction. As a result, the stock could move sideways until then. Of course, that doesn't impact our rating, which remains a Strong Buy; the benefits and synergies of the merger, coupled with the greater likelihood that AOL will come to reflect the value of it's telecommunications assets sooner with Time Warner than without them, keep AOL as a Strong Buy and one of the top companies in our universe.

-- FIRST CALL --

09:11am EST 11-Jan-00 Blair, William & Co. (Abhishek Gami) AOL AOL.RV
America Online Time Warner: Brand New (Pt 1 of 2)

William Blair & Company, L.L.C. Abhishek Gami (312) 364-8224

AMERICA ONLINE, INC. (AOL)

Price 1/11	Earnings Per Share			P/E Ratio		Div.	Yield	LTGR	Rating
$72 5/8	6/99	6/00E	6/01E	6/00E	6/01E	$0.00	0.0%	50%	"1"
($32-$95)	$0.17	$0.32	$0.44	NM	NM				

AOL Time Warner: Brand New

>>AOL's acquisition of Time Warner (TWX $92 1/4) is industry-defining and should lead to further online/offline marriages, but we believe that none could match AOL Time Warner's dominant position.

AOL Time Warner's global reach will be unparalleled, enhancing the company's ability to attract large advertisers and merchants to the multimedia platform.

The large premium AOL paid for Time Warner and the resulting combined valuation makes the upside for the stock in the near-term look less explosive than in the past. Over time, as the company rolls out new services that capitalize on its unique broadband strengths, we believe that the valuation could find room for further upside.

We expect that the largest acquisition in history will carry some integration and execution risks. We believe that the management of both companies are prepared to move quickly to start the integration process.

We like the deal and believe that investors should own the shares of AOL Time Warner--No. 1 teaming up with No. 1--when it closes in late 2000. In our opinion, AOL has gone from being the "first Internet blue-chip" to one of the most dynamic and important blue-chip companies in the market.

Recap

AOL will acquire Time Warner in an all-stock deal. Time Warner shareholders will receive 1.5 shares of AOL for every one of their shares, giving the acquisition an indicated value of approximately $163 billion based on AOL's closing price of $72.63. The deal will be accounted for as a purchase, resulting in approximately $150 billion to $155 billion in goodwill (assuming the deal closes at the current valuation) that will be amortized over 20 years. AOL shareholders will own 55% of AOL Time Warner after the acquisition closes, implying a $363 billion market cap for the new company. The exchange ratio is fixed and carries no collars, so by the time the deal closes, which we believe it will, in late 2000, the final valuation and goodwill amounts probably will differ from today's calculations.

Based on September figures, we estimate that the pro forma company is on a revenue run rate of approximately $32.75 billion and EBITDA of approximately $6.1 billion. The company believes that it will generate $10 billion in EBITDA on $40 billion in revenue during calendar 2001. We find this goal to be very reasonable and perhaps somewhat conservative.

Management

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We believe the new company's management team will be an important differentiating factor in its ultimate success. AOL's chairman and CEO, Steve Case, will become chairman of the new company. Time Warner's chairman and CEO, Gerald Levin, will serve as CEO of AOL Time Warner. AOL's president and COO, Bob Pittman, and Time Warner President Richard Parsons, will be co-COOs. Each company will place eight members on the board of directors. We think that Mr. Pittman will be particularly important in the integration efforts, as it was his "iron fist" that drove AOL to profitability and kept the company laser-focused on its profitable growth strategy. In addition, prior to joining AOL, Mr. Pittman spent part of his career working with Mr. Levin at Time Warner. AOL is deep in management talent at many levels of its organization and Time Warner (which also employs Ted Turner) is similarly a deep company with a long history of operations.

Brands and Cable Strategy

The management of both companies are strong proponents of multiple-brand strategies and the value of using massive distribution to generate revenues not only from self-created content, but also third-party content and service providers. The implications of this policy are that the company probably will allow other Internet service providers (ISPs) to buy access to the AOL Time Warner cable network to deliver Internet services, which AT&T (T $50 7/8) has refused to do until 2002. We think that there are considerable technological challenges that need to be solved, including the full upgrade of the Time Warner cable plant (scheduled to be completed by year-end 2000) before third parties can enter the market cost-effectively. Finally, we think that a market for premium Internet content could spring up. AOL Time Warner might be able to earn incremental fees from consumers who want to access certain types of content (for example, live concerts streamed online) for a small fee.

We believe that this deal is important from a cable aspect in more ways than merely enabling AOL to provide broadband Internet access. The combined company also will be able to offer telephony via cable, streaming audio, and streaming video. The ability to offer telephony via cable could provide AOL with a bargaining chip in stalled telephony negotiations with AT&T. For example, AOL could offer AT&T the ability to sell local telephony services over AOL Time Warner's cable lines in return for expedited access to AT&T's cable backbone for Internet connectivity.

Synergies

A few areas of cost efficiency and revenue enhancement jump out at us immediately, aside from the usual back-office reductions related to redundancies. AOL leads the Internet industry with approximately $1 billion in e-commerce and advertising revenue, but Time Warner's $5 billion in ad revenue dwarfs that. We believe that the combined entity will become much more efficient when it goes in to pitch advertisers because the Time Warner salesforce has existing relationships with many large advertisers (a number of whom probably are not investing much in Internet advertising) while AOL's sales force is expert in explaining the intricacies of the new medium. In addition, the combined salesforce may be able to cross-sell the online and offline media properties, leading to better sales and marketing cost efficiency. The combined company also should benefit from each firm's expertise in product development. AOL, for example, can learn a lot about creating and distributing Internet content via cable and for proper display on televisions. AOL also could benefit by using the Time Warner cable footprint to test out new broadband technologies. Time Warner, on the other hand, can cut back on the large amount of money it is spending to build an online brand. (The company has not found traction in the online market, despite spending millions of dollars on Pathfinder, only to shutter that operation recently and launch the new Entertaindom destination site.)

An intangible benefit that might accrue to the company includes the impact AOL's "paranoid" corporate culture could have as it rubs off on Time Warner's more mature corporate culture. Internet companies pride themselves on their ability to react very quickly to competitive threats, and throughout its history AOL often has acknowledged some level of anxiety about potential threats from Microsoft (MSFT $112 1/4), AT&T, and others. We believe that this healthy paranoia has helped to keep the company focused on its mission despite many challenges. As a slower-growing, semi-regulated company, Time Warner might benefit from AOL's "Internet fever." Of course the opposite could happen as well, but we believe that the top executives are strong, driven, goal-oriented leaders who have not yet created the final version of their vision. Bringing together and meshing AOL's 12,100 employees with time Warner's 70,000 employees will be one of the major challenges of this deal. The companies already have assigned a four-person transition team to take on the task. We expect there to be minimal headcount reductions (less than 10% of total personnel) due to normal overhead consolidation. We then expect AOL Time Warner to focus on improving productivity--something Mr. Pittman excels at doing.

Additional information is available upon request.

-> End of Note <-

09:12am EST 11-Jan-00 Blair, William & Co. (Abhishek Gami) AOL AOL.RV
America Online Time Warner: Brand New (Pt 2 of 2)

William Blair & Company, L.L.C. Abhishek Gami (312) 364-8224

AMERICA ONLINE, INC. (AOL)

Price 1/11	Earnings Per Share			P/E Ratio		Div.	Yield	LTGR	Rating
$72 5/8	6/99	6/00E	6/01E	6/00E	6/01E	$0.00	0.0%	50%	"1"
($32-$95)	$0.17	$0.32	$0.44	NM	NM				

Distribution
We believe that the combination of AOL's online distribution, brands, and network should boost the growth rates of Time Warner's content brands (for example: Time and People magazines, Time Life direct marketing, CNN, HBO, Warner Bros. Records, Atlantic Records, and a large library of digital media and trademarks). In the narrowband world, AOL's distribution capabilities encompass 135 million registered users of AOL, CompuServe, ICQ, Netcenter, Digital City, AOL MovieFone, and a number of emerging and related brands. This market-leading footprint should help Time Warner's dominant offline brands finally get a high profile on the Net. As we have seen in consumer e-commerce, offline brands (like barnesandnoble.com (BNBN $17), for example) can flourish online, but they are often slow to start and usually require a catalyst (often just large cash investments in the business) to achieve their potential. We believe that AOL can provide the catalyst Time Warner's properties have been looking for.

Time Warner is the world's largest media company, with in excess of 70 brands and brand extensions. Time Warner has 13 million cable household subscribers, 35 million HBO subscribers, 28 million print subscribers (representing 120 million readers), and other content brands that enter every home in the United States and millions more around the world. The company is strongest in cable, network television, publishing, and music. Time Warner's approximately 37% ownership stake (direct and indirect ownership) in the Road Runner broadband cable service provides AOL with a high-speed platform that passes in excess of 20 million homes. We estimate that nearly 600,000 homes have subscribed to the service so far, placing Road Runner behind Excite@Home (ATHM $40 1/8) as the largest cable Internet service in the world. We expect AOL to take advantage of this platform to distribute next-generation high-speed services like AOL TV at a premium to AOL subscribers. AOL also has an enormous opportunity to direct readers and viewers of Time Warner's properties back to AOL properties through integrated programming (for example, allowing HBO boxing viewers to score a fight on the AOL Sports channel). Combined with AOL's existing digital subscriber line (DSL) partnerships, the company now has much more control of its broadband future, although without some cooperation from AT&T/Excite@Home, AOL will have to wait until June 2002 to get nationwide cable Internet coverage.

AOL's ICQ brand is very strong overseas, as are Time Warner's properties, which could cause some conflicts with AOL's European joint ventures with Bertelsmann AG. Many of AOL's European operations are held in 50:50 joint ventures with Bertelsmann, which is one of the world's largest media companies as well and a direct competitor of Time Warner. Considering the growing maturity and strength of these international operations, plus growing interest for Internet investments in the European equity markets, we wonder if the companies will decide to spin the joint venture off into a publicly traded company. This also could give Bertelsmann a way to extricate itself from what could be an

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uncomfortable competitive situation.

Change the Game

We do not think that the end goal of the combined company is merely to improve cash flow, reduce costs, and leverage infrastructure. By bringing together the most powerful online and offline media companies, AOL Time Warner is reducing the friction that slows innovation. For example, aside from text-based communications, the Internet has not yet spawned what we call "made for medium content." Every medium has certain applications or programs that are best suited for it. We wonder if some sort of hybrid interactive video application (such as news programs that users can click on for specific pieces of deeper information in the context of the ongoing program) could be that killer application. Or perhaps the killer application will be fully immersive 3-D games and community environments.

Could the combined entity change how new music and videos are discovered, promoted, and distributed? On the Net, especially with broadband as an enabler, new artists can display their works and submit them for scrutiny from online talent scouts. By reducing the layers of complexity and procedure between publishers and artists, AOL Time Warner could help to reduce the existing barriers to launching new artists while improving the chances of success by using multiple media to deliver the new music or video in a controlled campaign.

We expect AOL Time Warner to help to create and shape this evolution in the medium by combining their unique technology, brand management, and distribution skills. By eliminating the competitive barriers that could slow both companies' ability to create, test, and deploy new next-generation services, we believe that the acquisition should lead to the creation of a unique media and communications entity.

Valuation

We believe there could be a natural turnover in the shareholder base of the combined company. At an indicated market cap of $363 billion, we believe that it will be difficult for AOL shareholders to enjoy the kinds of percentage returns they have been spoiled with during the past few years. In addition, AOL shareholders will no longer own an Internet "pure-play," which could temper their enthusiasm to some degree. On the other hand, Time Warner shareholders will be getting shares in a company that will need to continue to re-invest in growth and not merely increase its free cash flow. The higher valuation of the new company also may shake out some of the value-oriented investors in Time Warner's stock, as that stock had not performed well during 1999. The new stock probably will be more volatile than TWX but less volatile than AOL is currently. As some portion of the existing shareholder base cycles out, we think that a whole different set will cycle in. Investors who have been too afraid to buy into Internet pure-plays or those who felt that "old media" was threatened by new media might agree that AOL Time Warner is the best of both worlds. The net effect of this rotation probably will have minimal impact on the stock price once all is said and done, but in the interim, the stock could gyrate a bit as everyone plays musical chairs. Despite paying a significant premium to Time Warner's pre-acquisition price, as we posit above, we believe that there is a chance that AOL Time Warner will break new ground in consumer media, communications, and commerce, leading to higher valuations. We see no direct competitor to what will be the fourth-largest company in the world, and the vast majority of competitive scenarios we can think of in which a competitor tries to play catch-up by merging with other online/offline players do not seem

-- FIRST CALL --

08:56am EST 11-Jan-00 Bear Stearns (Jacobson/Lundin 212/272-6307) ERTS AOL TWX
AOL/TWX Merger Has Positive Implications-ERTS and Other Entertainment Companies

Marina K. Jacobson 212 272-6307 mjacobson@bear.com
Claire E. Lundin 212 272-4288 clundin@bear.com 01/11/00

Subject: Industry Overview
Industry: Entertainment/Specialty

BEAR, STEARNS & CO. INC.
EQUITY RESEARCH

AOL/TWX Merger Has Positive Implications for ERTS and Other Specialty Entertainment Companies

Key Points

*** The America OnLine/Time Warner merger announced yesterday underscores our belief that there is an increasing demand for proprietary entertainment content on the Internet.

*** The deal has the most direct implications for Electronic Arts, a leading independent game developer, which recently signed an exclusive five-year strategic agreement to exclusively program AOL's games sites (see our 11/22/99 note on ERTS for details of that agreement).

*** From a broader perspective, the merger has broad positive implications for the specialty entertainment companies we cover including Electronic Arts, Activision, Hasbro, Mattel, SFX, WWF Entertainment, and CINAR.

Benefits Of The AOL/TWX Merger For ERTS

Content, Content, Content. The merger could give ERTS an advantage or even proprietary access in licensing Time Warner's programming, magazine & book, film and music content for the AOL games site (which it will manage and generate profits from). This access could then allow ERTS to build up a mass-market "family entertainment" component to the games site in addition to its own sports, strategy, flight simulation, adventure and roll-playing content.

Quicker Road to Broadband. AOL's merger with Time Warner could expand the distribution of AOL's and therefore ERTS' Internet content. With this deal AOL increases its access to Time Warner's broadband platform through Time Warner's cable assets. Broadband technology helps increase the speed of game-play on the Internet and lessens the time it takes to download games (possibly benefiting ERTS' e-commerce effort as well). We expect almost all of EA.com's revenues of $15 million in fiscal 2000 (Mar) to come from subscriptions to "Ultima Online," ERTS' persistent state game "world" on the internet. As ERTS launches new persistent state games (five such games including "The Sims" are expected over the next several years), a larger portion of its total revenues should come from the highly lucrative subscription business (roughly 55% in 2001E) and a faster move to broadband should improve the playability of the games. In addition, increased penetration beyond the 8.9 million registered game users on AOL could help build advertising and e-commerce revenues on AOL and could help direct traffic to ERTS stand alone, EA.com site.

-- FIRST CALL --

Implications For Other Games, Toys And Entertainment Companies
Yesterday's announcement as well as other recent deals (EA/AOL, Hasbro/Go2Net, Lycos/Gamesville) help support our belief that proprietary entertainment content is becoming increasingly valuable for Internet companies. We would not be surprised to see other traditional media companies either get acquired by Internet companies or start to get highly compensated for the unique content and consumer interest (read: traffic and stickiness) they bring to the table.

As game and entertainment content has proven to be some of the most sticky content of the web, companies like Activision (a leading entertainment software company), CINAR (a leading children's entertainment and education company), Mattel (educational content from its acquisition of TLC), WWFE (a major draw for the highly coveted cohort of males 18-35) and SFX (proprietary access to premium event tickets and local entertainment) could be sought out for partnerships over the near term. Even HAS, which just formed a non-exclusive alliance with GNET could still see the value of its Internet content boost the overall valuation of the firm.

Deal Is Another Precursor for the Fight for the Living Room
Clearly Time Warner gives AOL increased access to the living room via cable distribution. We believe Sony is positioning its PlayStation II as a set-top box for the home with its Internet connectivity and DVD movie capability in addition to being a games machine. And, Microsoft is expected to enter the fray with its X-Box, which is believed to have comparable capabilities to the PlayStation II. From our perspective there are many players vying for access to the living room from many different angles, but any way it goes, the specialty entertainment companies have the content these players may need to get an edge.

Companies Mentioned: AOL, Time Warner, Activision, Mattel, Hasbro, SFX, CINAR, WWF Entertainment, Microsoft, Sony, Go2Net, Lycos

-> End of Note <-

07:31am EST 11-Jan-00 Robinson-Humphrey (RUSS 404 266-6143) AOL AOL.RV
AOL - Industry Implications of Merger with Time Warner

--SUMMARY--

* AOL's announced merger with TWX changes landscape of the entire Internet
* A company scoffed at by investors just two years ago has pulled-off the largest merger in history and becomes the company by which "new media" will be judged
* Most striking in the deal is the incredible distribution the combined company will have
* While others worried about AOL getting on "fat" cable pipes, AOL focused on assembling the best content for the broadband world. A strategy proving quite smart now that open access looks to be taking shape
* We now have the pioneer for the next chapter in the Internet's development--mainstream America going online
* Buy AOL shares and make them a core technology holding

--EARNINGS---

		FYE	1 Qtr	2 Qtr	3 Qtr	4 Qtr	Year
Actual	06/99	EPS	$0.02A	$0.04A	$0.05A	$0.06A	$0.17A
Previous	06/00	EPS	$0.07A	$0.07E	$0.08E	$0.08E	$0.30E
Current	06/00	EPS	$0.07A	$0.07E	$0.08E	$0.08E	$0.30E
Previous	06/01	EPS	$N/A	$N/A	$N/A	$N/A	$0.48E
Current	06/01	EPS	$N/A	$N/A	$N/A	$N/A	$0.48E
Previous	06/02	EPS	$N/A	$N/A	$N/A	$N/A	$N/A
Current	06/02	EPS	$N/A	$N/A	$N/A	$N/A	$N/A

Footnotes:

--FUNDAMENTALS---

Current Rating......:1
Risk Rank...........:Medium
P/E 06/00...........:242.1x
P/E 06/01...........:151.3x
Technical Rating....:1
ROE/LT Dbt-to-Cp....:5.50%/14.30%
Revenue.............:$4776.00 mil
Shares Outstanding..:2574.00 mil
Mkt. Capitalization.:$186949.62 mil
Comments............:

Price (1/10/2000)....:$72.63
12-Mo. Target Price.:$87.50
52 Wk Price Range...:$95.81 - $32.50
Proj. 5yr EPS Grth..:30.0%
Book Value(a)........:$1.49
Dividend/Yield.......:$0.00/0.00%
Latest Report Date..:Oct 20 1999
Convertible.........:Yes
Hedge Clause(s).....:

--OPINION--

AOL's announced merger with Time Warner yesterday threw the whole Internet industry into flux. The deal is a remarkable achievement for AOL, which less than two years ago was scoffed at by investors as a company toiling in the commodity business of Internet access. Now, the online pioneer has orchestrated the largest merger in history and soon will become the preeminent integrated media company by which "new media" will be judged.

Most striking in this deal is the distribution this combined company will

-- FIRST CALL --

have when the merger is complete. The incredible laundry list includes: 20 million online AOL subscribers, 120 million readers of Timer Warner print properties, 20 million homes passed with cable, 35 million HBO subscribers, 75 million homes receiving TBS and TNT and nearly 1 billion people worldwide with exposure to CNN. The numbers are truly staggering.

Most interesting about the deal is how it changes the competitive landscape. Near-sighted investors have focused almost exclusively on high-speed Internet access and the supposed monopoly of AT&T/@Home. They said if AOL could not get to AT&T's pipes, then they would fail in the broadband future. While investors worried, AOL formulated a strategy focused on acquiring the right content and brands that would be invaluable once open access occurred. You see, fat pipes aren't much of an asset unless there is compelling content to put over them. Once the open access obstacle was removed (when AT&T recently announced it would adopt an open access stance in the future), then it was time to assemble the content. Did it ever, with an arsenal unmatched in the B&M and Internet world.

So what we have now is a pioneer for the next chapter of the Internet; one in which we believe AOL will facilitate the adoption of the Internet by mainstream America. The combined company arguably has a "touch-point" to the entire United States population in one form or another and this will prove invaluable in fostering Americans into the online world. We have argued in the past that a traditional media strategy for attracting the next wave of Internet users (post early adopters) was key for Internet success, and we believe that AOL validated this idea yesterday.

If you don't already own AOL shares, buy them now and make them a core technology holding in an investor's portfolio. Own the company that will help to define how media is delivered in the futre, whether it be print, TV or Internet.

RATING = Robinson-Humphrey's rating system assigns a number code (1 = BUY, 2 = OUTPERFORM, 3 = NEUTRAL, 4 = UNDERPERFORM, 5 = SELL) for our 12 month fundamental rating as well as for our technical ratings. Our BUY and OUTPERFORM ratings indicate that we expect the stock to beat appropriate market indices over the next twelve months. A NEUTRAL rating suggests in line with market-type performance. Our UNDERPERFORM and SELL rating indicate underperformance is expected over the next twelve months. Also included is our risk rating: L = Low, M = Medium, H = High, S = Speculative. All references to the ratings appear in the following order: fundamental -- risk rank-- technical.